



February 16, 2017

Proposed SEC Rules Requiring the Use of Universal Proxies

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On October 26, 2016, the U.S. Securities and Exchange Commission (SEC) proposed new rules under the *Securities Exchange Act of 1934*, as amended (Exchange Act), that would require parties soliciting proxies in contested director elections to use universal proxies listing all the nominee director candidates for whom proxies are being solicited. The purpose of the proposed rules is to have the proxy voting process better mirror the in-person voting process that takes place at shareholders' meetings so that shareholders voting by proxy may vote for any combination of the registrant and dissident nominees. The proposed rules apply only to registrants that are subject to the U.S. federal proxy rules and, therefore, will not affect foreign private issuers, including Canadian public companies with securities listed on a U.S. stock exchange.¹

The Existing Proxy Rules: Limited Shareholder Choice in Contested Director Elections

The choices of shareholders voting by proxy in contested director elections are limited for two main reasons.² First, under the current proxy rules, a proxy may confer authority to vote only for a "bona fide" nominee, defined as a nominee who has consented to being named in the proxy statement and to serve if elected. Hence, one party may not include the other party's nominees on its proxy card unless the other party's nominees consent. Director nominees may (and often do) withhold their consent from being listed on opposing parties' proxies. The reasons for withholding consent include, in part, a perceived advantage in forcing shareholders to choose between competing slates of nominees, and avoiding the appearance of supporting the opposing party's position. Second, shareholder choice in contested director elections is limited because the existing proxy rules do not require either party to include the other party's director nominees on its proxy card. Therefore, even if a nominee consents to being named on the other party's proxy card, the other party can (and often will) determine not to include the nominee on its proxy card, since there is rarely an incentive to do so.

As a result, proxy cards in contested director elections typically present the registrant's director nominees as one slate in the registrant's proxy statement and proxy card, and the dissident's

¹ The proposed universal proxy rules apply only to registrants with securities registered under section 12 of the Exchange Act that are subject to U.S. federal proxy rules. Registrants with reporting obligations only under Exchange Act section 15(d) and foreign private issuers are not subject to the federal proxy rules and, therefore, will not be subject to the proposed rules.

² Contested elections are director elections in which a person or group of persons is soliciting proxies in support of director nominees other than the registrant's nominees.

director nominees as a separate (full or partial) slate in the dissident's proxy statement and proxy card. Shareholders voting by proxy generally may not submit two separate proxy cards, so such shareholders are often forced to vote for the registrant's director nominees to the exclusion of the dissident's director nominees, or vice versa. In contrast, shareholders voting in person generally have the freedom to vote for a combination of the registrant's and dissident's director nominees by casting a written ballot provided at the meeting that includes the names of all duly nominated candidates.

The Proposed Rules: Universal Proxies

The proposed rules would require parties to provide shareholders voting by proxy with universal proxy cards in all non-exempt solicitations in connection with certain contested elections.³ The universal proxy cards provided to shareholders will include the names of all duly nominated director candidates for whom proxies are solicited (clearly distinguishing between the registrant and the dissident nominees on the proxy cards) so that shareholders voting by proxy may vote for any combination of the registrant's and dissident's slates.

To facilitate the use of universal proxies, the SEC is proposing to expand the definition of "bona fide" nominee to a nominee who has "consented to being named in a proxy statement relating to the registrant's next annual meeting of shareholders at which directors are to be elected [...] and to serve if elected." Therefore, once a nominee has consented to being named in a party's proxy statement, other parties can list the nominee in their own proxy statements without needing to solicit further consent from the nominee.

The proposed rules include notice requirements that facilitate the universal proxy regime. The dissident would be required to notify the registrant of the names of its nominees no later than 60 calendar days before the anniversary of the previous year's annual meeting date.⁴ The registrant would be required to notify the dissident of the names of its nominees no later than 50 calendar days before the anniversary of the previous year's annual meeting date. Additionally, the dissident would be required to file its definitive proxy statement by the later of 25 calendar days before the meeting date or five calendar days after the date when the registrant files its definitive proxy statement.

If a registrant discovered after disseminating its definitive proxy statement with a universal proxy card that a dissident failed to file its definitive proxy statement 25 calendar days before the meeting (or five calendar days after the registrant filed its definitive proxy statement), the registrant could elect to disseminate a new, non-universal proxy card including only the names of the registrant's nominees.

³ Non-exempt solicitations conducted by registered investment companies and business development companies would not be affected by the proposed rule.

⁴ If the registrant did not hold an annual meeting during the previous year, or if the date of the meeting has changed by more than 30 calendar days from the previous year, then notice must be provided by the later of 60 calendar days before the date of the annual meeting or 10 calendar days following the day on which public announcement of the date of the annual meeting is first made by the registrant.

“Vote No” Campaigns

The proposed rules do not apply to proponents conducting a solicitation without a competing slate, such as a “vote no” campaign (where a soliciting person is soliciting only “withhold” or “against” votes with respect to one or more of the registrant’s nominees) or a solicitation where a shareholder is soliciting proxies only in support of a shareholder proposal. Those solicitations have no alternative director nominees, and so they would not raise the same concerns that mandatory universal proxy is intended to address, because the registrant’s proxy card already provides shareholders with the ability to select their choice of nominees from all director candidates.

Solicitation Requirement

To prevent a “free rider” benefit, where dissidents capitalize on the registrant’s solicitation efforts, the dissident would be required to solicit the holders of shares representing at least a majority of the voting power entitled to vote on the election of directors. The mandatory universal proxy requirement would be triggered only by a dissident that conducts a separate solicitation by distributing its own proxy statement and form of proxy. The proposed rules would also require a dissident to state in its proxy materials that it will solicit the holders of shares representing at least a majority of the voting power entitled to vote on the election of directors.

Where a dissident fails to comply with the proposed rules, the dissident would not be permitted to continue with its solicitation under Regulation 14A. Because a registrant may disseminate a universal proxy card before discovering that a dissident is not proceeding with its solicitation, the proposed rules require the registrant to include disclosure in its proxy statement advising shareholders how it intends to treat proxy authority granted in favour of a dissident’s nominees if the dissident abandons its solicitation or fails to comply with the proposed rules.

Elimination of the “Short Slate Rule”

The SEC is proposing to eliminate the “short slate rule,” adopted in 1992. That rule applies only to a dissident seeking to elect a minority of the board in an election contest and permits the dissident to “round out its slate” by soliciting proxy authority to vote for some of the registrant nominees, other than those registrant nominees that the dissident has specified on its proxy card that the dissident will *not* vote for. While the short slate rule enables shareholders to use a proxy card to vote for all board seats up for election, the *dissident*, rather than the *shareholder*, chooses the nominees. Under the proposed rules that mandate universal proxies, shareholders will be able to vote on the universal proxy card for all board seats and select their own preferred combination of nominees from all registrant and dissident nominees. Therefore, the short slate rule would no longer be necessary to ensure that shareholders voting for a dissident’s partial slate would have the opportunity to vote for a full slate of directors.

Voting Options and Voting Standards

The SEC has also proposed “clean-up” amendments to the form of proxy card and proxy statement disclosure requirements with respect to voting options and voting standards, in response to concerns that some company proxy statements had ambiguities or inaccuracies in their disclosures about voting standards in director elections. Specifically, the proposed rules would (i) require that proxy cards include an “against” voting option when applicable state laws give effect to a vote against; and (ii) give shareholders who neither support nor oppose a

director nominee an ability to “abstain” (rather than “withhold authority to vote”) in a director election governed by a majority voting standard. Finally, the proposed rules would mandate disclosure in proxy statements about the effect of a “withhold” vote in an election.

Differences Between the Universal Proxy System and Proxy Access

The proposed mandatory universal proxy system differs in significant respects from proxy access because it would not provide shareholders or their nominees with access to a registrant’s proxy materials in the same manner and extent provided by proxy access bylaws.

Proxy access bylaws commonly require the registrant to include in its proxy statement the names of the nominating shareholder’s nominees, disclosure required by Schedule 14A about the nominating shareholder and its nominees, and a statement provided by the nominating shareholder in support of its nominees’ election to the board. Nominating shareholders complying with proxy access bylaws are not required to prepare and file their own preliminary and definitive proxy statements or disseminate any proxy material or solicit any shareholders. Information about their nominees is included in the registrant’s proxy materials and provided to shareholders along with the registrant’s proxy card listing the names of the nominating shareholder’s nominees.

In contrast, the proposed mandatory universal proxy system would require only that the registrant include the names of the dissident nominees on its proxy card. No other disclosure about the dissident’s nominees would be required by the registrant. The dissident would be wholly responsible for disseminating information about its nominees to shareholders and soliciting proxies in support of its nominees. The dissident’s “access” in the proposed mandatory universal proxy system would be limited to the listing of nominee names on the proxy card and would be accompanied by the obligation to solicit on behalf of its own nominees.

Furthermore, as discussed above, the proposed mandatory universal proxy system would apply only in solicitations with a competing slate, and therefore, in an election of directors involving only registrant and proxy access nominees, the universal proxy system would not apply. In this type of solicitation, proxy access already provides shareholders voting by proxy with access to a proxy card that reflects all of their voting options for the election of directors.

If you have any questions regarding the foregoing, please contact [Jeffrey Nadler](mailto:Jeffrey.Nadler@dwpm.com) (212.588.5505) or [Scott D. Fisher](mailto:Scott.D.Fisher@dwpm.com) (212.588.5596) in our New York office.

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